BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

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PETITION FOR MODIFICATION OF D.04-12-048 OF THE ENERGY PRODUCERS AND USERS COALITION

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PETITION FOR MOFICIATION OF D.04-12-048 FOR THE ENERGY PRODUCERS AND USERS COALITION

I. PROCEDURAL GROUNDS FOR PETITION

Pursuant to Rule 16.4 of the Commission's Rules of Practice and Procedure, the Energy Producers and Users Coalition (EPUC)[1] brings this petition to modify D.04-12-048. This petition also seeks modification of all subsequent procurement decisions implementing certain nonbypassable charge (NBC) policies adopted in D.04-12-048[2] and applicable to customer generation departing load (CGDL).[3] Specifically, modification is sought to address the imposition of an NBC on CGDL to permit recovery by the utility of ongoing utility

[1] EPUC is an ad hoc group representing the electric end use and customer generation interests of the following companies: Aera Energy LLC, BP America Inc. (including Atlantic Richfield Company), Chevron U.S.A. Inc., ConocoPhillips Company, ExxonMobil Power and Gas Services Inc., Shell Oil Products US, THUMS Long Beach Company, Occidental Elk Hills, Inc., and Valero Refining Company – California.

[2] D.03-12-059 (approving SCE acquisition of Mountainview); D.04-06-011 (approving San Diego Gas & Electric Company's Reliability RFP); D.06-06-035 (approving Joint Settlement Agreement, as modified, for PG&E acquisition of Contra Costa 8); D.06-07-029 (approving Procurement NBC for net capacity costs associated with power purchase agreements for PG&E and SCE); D.06-11-048 (approving PG&E Long Term Request for Offer Results).

[3] "Customer generation" includes cogeneration, renewable technologies such as solar panels, fuel cells or any other type of generation that is constructed with private investment capital and is dedicated wholly or in part to serve a special customer's load. "Customer generation" typically serves load relying on privately funded distribution wires, rather than relying on the utility grid.

procurement costs incurred in the normal course of business ("Procurement NBC").

The Petition meets the requirements of Rule 16.4 in several ways. First, three of the decisions for which modification is sought were issued within the past year: D.06-06-035; D.06-07-029; and D.06-11-048. Second, EPUC previously sought the requested modification to D.04-12-048 through a timely filed Application for Rehearing,[4] which was rejected by the Commission in D.05-09-022. The decision rejected the Application on grounds that EPUC had not specified legal error, but observed that the arguments made were policy arguments. Consequently, and in light of the increasing adoption of facility-specific and more generic Procurement NBCs[5], EPUC now brings its request to the Commission as a Petition for Modification based on policy grounds.

Third, California has a continuing need for electricity supply. This fact, combined with recent affirmation by the California Energy Commission (CEC or Energy Commission) and this Commission of State policy favoring cogeneration, compel reexamination of the Commission's NBC policy. It must be ensured that this policy does not discourage cogeneration development.[6] Fourth, certain

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[4] On January 18, 2005, CAC/EPUC filed an application to rehear D.04-12-048 (Application to Rehear). The basis of the application was, among other reasons, to address the imposition of net stranded costs on all customers, including through the use of any surcharge on the right of cogeneration facilities to engage in customer generation.

[5] *See, e.g.,* D.06-06-035, at 10 ("*Commission decisional precedent supports the ten-year stranded cost recovery*.")

[6] President Peevey's Ruling, issued in Rulemakings 05-12-013 and 06-02-013 (August 15 Peevey Ruling), and D.06-07-029, issued on July 20, 2006, demonstrate the changed circumstances now faced by this Commission and California ratepayers. The Commission may take official notice of its own issuances stressing the unexpected need for additional generating capacity to meet the State's growing demand. *See* Commission Rules of Practice and Procedure, Rule 13.9. "*Last month's heat storm [July 2006], and the evident and surprising*

EPUC members are now considering the development of new and repowered cogeneration facilities to serve the electrical demand of California refineries. These operations require greater certainty in the range of applicable NBCs to CGDL in order to reasonably assess their options.

II. REQUEST FOR COMMISSION ACTION

EPUC seeks clarification of D.04-12-048 and the subsequent decisions in two respects. First, EPUC requests that the Commission confirm the investor-owned utilities (IOUs) obligation to maintain their long-standing practice of forecasting CGDL when procuring power to meet native load. Second, EPUC requests a ruling by the Commission that a Procurement NBC, resulting from the IOUs' ongoing procurement activities in the normal course of business, may not be applied to CGDL. Requiring developers of new cogeneration projects to pay both for their own capital investment and the utilities' ongoing capital recovery is unreasonable and will discourage further cogeneration development.

EPUC bases this request on solid policy grounds. As explained below, CGDL NBCs create material uncertainty for industrial consumers considering the installation of new or repowered cogeneration facilities and unnecessarily burden the economics of potential projects. Minimizing these impacts by eliminating the Procurement NBC for CGDL would offer the following array of benefits.

- Lifting the burden of the Procurement NBC would increase the likelihood of project development.

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growth in demand that had occurred even before the heat storm, give rise to the need for further action." August 15 Peevey Ruling, at 3. The changed circumstances highlighted by these Commission issuances render this petition timely, as do the current considerations for development of new or repowered facilities.

- Increased on-site cogeneration development offers reliability benefits to the grid and benefits utility ratepayers in the event of outages by adding reliable, California-dedicated power supplies.

- Increased cogeneration development would benefit the State by decreasing the State's greenhouse gas (GHG) emissions inventory and increasing the level of energy efficiency.

- Increased cogeneration reduces the burden on utility investment, helping to reduce ratepayer costs.

Any cost-shifting concerns related to the elimination of the Procurement NBC for CGDL customers should be assuaged by prudent utility planning and the inclusion of CGDL in utility forecasts. For all of these reasons, the Commission should grant this Petition.

III. THE EVOLUTION OF NBC POLICY WARRANTS THE COMMISSION'S CAREFUL REVIEW.

A. The Origins Of NBC Policy Warrants The Commission's Careful Review

Nonbypassable CGDL charges (often referred to as "exit fees") are a creation of relatively recent regulatory policy. Before the introduction of retail competition in California under Assembly Bill 1890, the IOUs planned for the procurement of power, accounting for departing load with little apparent problem. The IOUs planned their businesses to foresee and accommodate certain changes of their customers in the normal course of business, whether projected load growth or load leaving the system through plant closures or the installation of customer generation. In fact, there is no indication that the IOUs encountered difficulty in procurement planning even in the face of the Public Utility Regulatory Policies Act of 1978 (PURPA), which resulted in thousands of megawatts (MW) of new on-site cogeneration and a material increase in departing load. The

Federal Energy Regulatory Commission (FERC) perhaps said it best in adopting its stranded transmission cost policy in Order 888. FERC stated:

> *this Rule will not insulate a utility from the* ***normal risks of competition****, such as self-generation, cogeneration or industrial plant closure, that do not arise from the new availability of nondiscriminatory open access transmission. Any such costs would not constitute stranded costs for the purposes of this Rule.*[7]

The landscape seemed to change, however, when California began to contemplate retail competition, or Direct Access. With the advent of Direct Access, the IOUs feared that customers would leave their system to be served by energy service providers (ESPs), leaving the IOUs with "stranded capacity" and associated costs. [8] Consequently, both this Commission and the Legislature developed a NBC structure to ensure that any then-stranded costs would be recovered through the transition to retail competition.[9] This NBC, labeled the "Competition Transition Charge" (CTC) was designed to recover the uneconomic portion of the utilities ongoing generation costs left "stranded" by the migration of regulatory policy to include Direct Access. The primary target of this charge was new Direct Access load. Recognizing the history and benefits of cogeneration in

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[7] Order No. 888, Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Service by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, 61 Fed. Reg. 21,540, FERC Statutes and Regulations, Regulations Preambles January 1991 – June 1996, 31,036 (1996), order on reh'g, Order No. 888-A, 62 Fed. Reg. 12,274, FERC Statutes and Regulations 31,048 (1997), order on reh'g, Order No. 888-C, 82 FERC 61,046 (1998).

[8] *See* 64 CPUC 2d 1, 1995 WL 792086 (Cal.P.U.C.) (D.95-12-063) ("*The policy decision recognizes that the introduction of retail competition could result in stranded costs -- i.e., in a utility being unable to completely recover the costs of its facilities and contracts in the market*.")

[9] *See* West's Ann.Cal.Pub.Util. Code P.U. Code § 367; *see also* D.95-12-063.

the state, and implicitly acknowledging them, cogeneration was largely exempted from CTC.[10]

The Commission's NBC policy then moved on to address a new type of costs, arising not in the normal course of business, but under unique circumstances. In the wake of the 2000-01 energy crisis, the IOUs and the State incurred unanticipated costs and took on high-priced obligations to keep the lights on. The Commission created new NBCs to provide for recovery of these costs from customers for whose benefit the costs were incurred.[11] Costs resulting from "water under the bridge" crisis purchases were spread to virtually all customers connected to the grid during this period through the nonbypassable California Department of Water Resources (CDWR) Bond Charge.[12] Costs associated with the future obligations undertaken by CDWR during the crisis, however, were allocated with greater precision, employing long-standing principles of cost-causation. [13] CDWR did not incur costs for 3000 MW of CGDL.[14] Specifically, the Commission acknowledged that the IOUs plan for CGDL and, indeed, planned for CGDL in developing the demand forecast used

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10 *See* West's Ann.Cal.Pub.Util. Code P.U. Code § 372.

11 *See, generally,* D.03-04-030.

12 *See Id*., at 41, 57.

13 *See Id., at 54 ("It is clear that DWR, when negotiating long-term power contracts, assumed that a certain amount of customer generation departing load would occur every year and therefore did not procure long-term power for that portion of the load. In fact, such an assumption is based on common sense, since utilities have always faced departing load in various forms, including that caused by an economic downturn, improvements in energy efficiency and building codes, as well as installation of self-generation systems.")*

14 *See* D.03-04-030, FOF 11, FOF 20 at 60-61; *see also* D.05-09-022, at 8.

by the CDWR in procuring during the energy crisis.[15] On that basis, the Commission carved out 3000 MW of exemptions for CGDL from the CDWR ongoing power charges. The exemption lasts for the entire terms of the CDWR power contracts, through 2015.[16]

B. A Shift in NBC Policy: Utility Investment In The Normal Curse Of Business

Aware of the Commission's growing openness to NBCs, the IOUs turned from requesting approval of NBCs for unique circumstances – *e.g.,* retail competition transition and energy crisis – to asking for NBCs for activities undertaken in the normal course of business. In Decision 04-12-048, at issue in this petition, the Commission authorized the IOUs to plan and procure the resources necessary to serve load projected for the 2005-2014 period.[17] The decision not only authorized the IOU's procurement plans, it also authorized the IOUs to recover any stranded costs through a Procurement NBC.

This Procurement NBC could be assessed on departing load over the life of the contract or 10 years, whichever is less.[18] It also authorized cost recovery for utility-owned generation acquired as a result of the procurement process.[19] Thus these charges include procurement contract expenses as well as the

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15 *See* D.03-04-030, at 54 ("*we will simply rely on the DWR/Navigant model assumptions to set one overall cap of 3,000 MW (the approximate cumulative total (rounded) of DWR's annual assumptions over ten years) We will apply this cap to all CG departing load.")*

16 *Id; see also* D.06-07-030, at 21-22, footnote 24 ("*Although the last DWR contract does not expire until 2015, the vast majority of contracts expire by 2011.*")

17 *See,* D.04-12-048, at 2.

18 *See,* D.04-12-048, COL 16, at 229-230.

19 *Id, at 61.*

expenses incurred by an IOU in procuring its own generation resources.[20] The Decision speaks about load uncertainty faced by the IOUs specifically in terms of Community Choice Aggregation (CCA), municipal departing load, and the possible revival of Direct Access.[21] Notably, CGDL is not mentioned in the list of potential causes for load uncertainty.[22]

The first application of the Procurement NBC arose in the context of SCE's acquisition of the Mountainview facility. In D.03-12-059, the Commission authorized SCE to charge its customers for potential stranded costs associated with its Mountainview facility for a 10-year period. In D.04-06-011, the Commission granted permission to San Diego Gas & Electric Company for a

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20 *Id.*

21 See D.04-12-048, at 55 (in the section "***Potential Stranded Costs Due to Customer Load Uncertainty****",* the decision states*:* "*The implementation of CCA, departing municipal load, and the potential for lifting, in some form or another, the current ban on allowing new DA all create a great degree of uncertainty as to the amount of load the existing utilities will be responsible for serving in the future.*")

22 *See* Id. In fact, D.04-12-048 actually **affirms** that the IOUs are supposed to be planning for CGDL and reducing their load forecasts accordingly. "*[E]ach IOU prepared a DG [Distributed Generation] forecast that is based on a forecast of DG operating on the customer-side of the meter.* ***These estimates are then deducted from the load forecast****… This resource counting protocol recognizes that customer-side DG reduces the utility's actual load to be served and the associated reserve margin attributed to that self-served load.*" D.04-12-048, at 70-71 (emphasis added). Despite this clear direction to the IOUs to continue to forecast CGDL in D.04-12-048, the IOUs were also authorized to assess Procurement NBCs on CGDL. D.06-11-04 similarly states that customer generation was considered in the utilities lead forecasting and planning process: "*Taking into account…combined heat and power on-site generation incentives, the long-term procurement plan adopted for PG&E established that there is a need for 2,200 megawatts(MW)of new generation in northern California by 2010*." D.06-10-048 at 2. Notably, Commissioner Peevey's recent draft decision in R.06-03-004 defines DG first and foremost by its proximity to load: "*DG is a parallel or stand alone electric generating unit generally located within the electric distribution system* ***at or near the point of consumption*****.**" Peevey Proposed Decision, issued Dec. 6, 2006, at 4. It would be illogical for the Commission to order utility forecasting of small DG facilities and exclude from utility forecasting larger cogeneration facilities.

similar NBC associated with its Reliability RFP; this NBC was limited to 10-years or the life of the contract, whichever is less.[23]

D.04-12-048, however, was the first decision to broaden and deepen the application of the Procurement NBC. D.04-12-048 grants authority for assessment of Procurement NBCs on departing load to all three IOUs and for recovery of both long-term procurement contracts costs and utility-owned generation costs.[24] The Procurement NBC has since been advanced further over the past two years in the Commission's adoption of facility-specific 10-year nonbypassable charges for PG&E. The Commission has approved Procurement NBCs for PG&E's acquisitions of Contra Costa 8 (CC8) and Wartsila Humboldt. PG&E may also assess a Procurement NBC to recover costs associated with its Purchase and Sale Agreement (PSA) for E&L Westcoast Colusa, a 657 MW facility; moreover, PG&E has been authorized, at some future date, to elect to allocate net capacity costs associated with five power purchase agreements to CGDL through a Procurement NBC.[25]

In the case of CC8, a 530 MW facility, PG&E first requested a 30-year Procurement NBC for CC8. Despite the multiple implementation details left inchoate, the Commission approved a 10-year Procurement NBC for this

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[23] Importantly, this decision refers specifically to application of the NBC in the context of Direct Access: "*all customers of SDG&E that are currently ineligible for **direct access** are obligated to pay for the stranded costs of any new generation for the next ten years*. *This will insure that neither the utility nor its bundled customers, will be forced to pay stranded costs for these generation assets in the event that **new direct access** is permitted*." D.04-06-011, at 42 (emphasis added).

[24] See D.04-12-048, at 61, COL 16.

[25] *See* D.06-11-048, at 35, COL 25.

"relatively low-cost and low-risk" facility.[26] It bears noting that PG&E has since increased the capital cost estimate significantly by $75 million.[27, 28] Similarly, the Commission approved PG&E's request for authority to assess a Procurement NBC to recover costs associated with the acquisition of the 163 MW Wartsila Humboldt plant and with the Colusa PSA.[29]

Decision 06-07-029, adopted July 20, 2006 -- the Phase I decision issued in the long-term procurement proceeding (R.06-02-013) – also expanded the Procurement NBC. This decision concludes that California needs new generation.[30] In particular, it finds that PG&E has a need for 2,200MW of new generation and SCE has a need for 1,500 MW of new generation.[31] Accordingly,

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[26] *See* D.06-06-035, FOF 10, at 20.

[27] *See* PG&E Advice Letter 2928-E seeking approval of a $75 million increase in capital cost and the resulting revenue requirement for Contra Costa 8.

[28] Contemporaneously with PG&E's application for a 30-year Procurement NBC for CC8 (A.05-06-029), SCE requested approval for a Procurement NBC to be applicable not only to customers located in its service territory, but also to customers throughout southern California (A.05-06-003). On June 2, 2005, SCE filed an application for approval of Power Purchase Agreements (PPAs) secured through its April RFO; the April RFO was for new long-term PPAs for 1500 MW of new generation. According to SCE, the PPAs would facilitate construction of new power generating units in South of Path 15 (SP-15) to mitigate the potential for grid unreliability due to resource insufficiency. SCE amazingly proposed that the costs of the contracts exceeding the market value of the energy would be recovered from ***all*** SP-15 electricity consumers. SCE asserted that all consumers, including those served by Energy Service Providers (ESPs), Community Choice Aggregators (CCAs), and by self-generation, benefited from the increased resource supply and reliability in SP-15.

Importantly, the Assigned Commissioner's Scoping Memo and Ruling limited the proceeding to a consideration of only SCE's asserted need to procure 1000 MW for its bundled load. This limitation excluded any issues about meeting the requirements of non-utility load served by ESPs and CCAs, eliminating the risk of departing load "exit fees." SCE subsequently terminated the RFO and filed a motion to withdraw the application, characterizing the order as "rejecting" SCE's proposal to meet the needs of all of SP-15. The motion was granted.

[29] *See* D.06-11-048, at 35, COL 24, OP 23.

[30] D.06-07-029, at 55 (Findings of Fact ¶¶12-14).

[31] Id., at 54 (Finding of Fact ¶4).

it authorizes PG&E and SCE to procure these amounts of generation and to recover the net capacity costs through Procurement NBCs as authorized by D.04-12-048.[32]

The focus of this Petition rests not on the NBCs adopted under the extraordinary circumstances of retail transition or the energy crisis. Rather, this Petition focuses on the more recent Procurement NBCs that the Commission has permitted the utilities to impose to cover their planning in the normal course of business. The cumulative effect of all of the NBCs, combined with the complete lack of concrete notice of the new Procurement NBC, is to discourage the development of new, efficient cogeneration facilities to meet the state's electricity demand. As a matter of policy, the Commission should prohibit the IOUs from applying Procurement NBCs to impose utility investment costs on entities willing to invest private capital in new customer generation facilities.

IV. THE COMMISSION SHOULD MODIFY PRIOR DECISIONS TO CLARIFY THAT THE PROCUREMENT NBC SHOULD NOT BE APPLIED TO CUSTOMER GENERATION DEPARTING LOAD.

The appropriateness of any NBC in the ordinary course of utility procurement planning is questionable. The burgeoning NBC burden effectively relieves the IOUs of responsibility for prudent procurement planning – a responsibility they have shouldered for decades and should continue to bear. The IOUs have a reasonable opportunity with proper planning tools to anticipate load increases and decreases in the normal course of business, absent unusual and unforeseeable circumstances.

[32] Id, at 56-57; *see also* D.06-11-048, at 35, COL 24, OP 23..

A reasonable course of action under the circumstances would be to eliminate the Procurement NBC entirely. This Petition, however, does not ask the Commission to go that far. Instead, the Petition requests that the Commission confirm again the IOUs' obligation to plan for CGDL, as they have done in the past,[33] and bar the application of the Procurement NBC to these customers.

Burdening the development of new cogeneration facilities or the repowering of existing facilities, by a significant and unpredictable Procurement NBC is not in the State's best interest. The State has a strong history of self-generation and cogeneration. Further, now, more than ever, California needs new energy-efficient generation facilities. In-state cogeneration facilities provide California-dedicated reliability and supply benefits. Cogeneration facilities also impact GHG emissions inventory goals and can help reduce the burden on utility investment. Together, these facts call for a shift in Commission policy on application of Procurment NBCs to CGDL.

A. Procurement NBCs Decrease The Likelihood Of Installation Of New Or Repowered Cogeneration Facilities Through Increased Uncertainty And Unreasonable Burdens On Project Economics

Decision 04-12-048 and D.05-09-022 both dismiss arguments that the imposition of Procurement NBCs on cogeneration facilities is inconsistent with the state's policy to encourage their operation and use. EPUC acknowledges that the Commission's imposition of NBCs is not explicitly directed to discourage cogeneration. EPUC also recognizes that many other factors come into play

[33] D.04-12-048 itself states that the IOUs are supposed to plan for Distributed Generation and reduce their load forecasts accordingly. *See* D.04-12-048, at 70-71; *see also* D.03-04-030, at 54.

when assessing the viability of a cogeneration project. Nonetheless, imposing Procurement NBCs is contrary to sound, established State policy on cogeneration and unnecessarily burdens project development. Procurement NBCs both impede project planning and undermine project economics; these added, unwarranted burdens significantly increase financial uncertainty, making eventual project development far less likely.

1. CGDL Customers Are Unable to Properly Assess Project Economics With The Unknown and Unknowable Burden of Procurement NBCs

The failure to quantify NBCs and provide customers sufficient notice of their impact severely strains the customer's decisionmaking process for customer generation projects. Today, certain NBC "exit fees" are known, and others are not. Moreover, even where an NBC is known, it may be subject to material change over time. Further, each NBC on its own may represent an added expense large enough to derail otherwise viable projects.

a. CGDL Projects Are Currently Burdened by Numerous NBCs.

The existing CGDL NBCs applicable to customer generation facilities that depart utility service to engage in self generation are numerous. They include:

(1) CDWR Bond Charge;[34]
(2) CDWR Power Charge indifference adjustment;
(3) Competition Transition Charge (CTC);
(4) Nuclear Decommissioning Charge (NDC);
(5) Regulatory Asset Charge (PG&E Only);
(6) Public Purpose Program Charge (PPP);

[34] *See* PG&E Schedule E-DCG Departing Customer Generation, CG Rates; SCE Schedules CGDL-CRS Customer Generation Departing Load Cost Responsibility Surcharge and DL-NBC Departing Load Nonbypassable Charges for list of CGDL NBCs. Note that SCE combines the DWR charges, CTC and HPC charges into the Cost Responsibility Surcharge (CRS).

(7) Trust Transfer Amount Charge; and
(8) Energy Cost Recovery Amount (ECRA).

These NBCs range in materiality and predictability. Each is subject to change over time. For example, take just one component of the PPP, the California Alternative Rates for Energy (CARE) program.[35] CARE is a low-income assistance program that provides a rate discount to low-income households. The revenue shortfall associated with the CARE program discount is recovered from all ratepayers, except CARE participants and streetlighting customers. In 2001, the combined CARE program for all three investor owned utilities (i.e, SCE, SDG&E and PG&E) totaled about $140 million. In contrast, PG&E's CARE rates proposed in A.06-03-005, PG&E's 2007 General Rate Case, have substantially increased and reflect total program costs for PG&E alone of over $322 million for one year. Moreover, the Commission's recently adopted budget for the CARE program for 2007 is $977.4 million. CARE is not the only escalating component of the PPP charge. Implementation of the California Solar Initiative will add approximately $2.8 Billion in costs to the PPP revenue requirement, causing further, dramatic increases to the PPP NBC.

The below table quantifies current CGDL NBCs. Notably, the amounts of the Procurement NBCs remain unknown.

[35] EPUC is **not** stating that CGDL customers should not pay any PPP charges; rather, EPUC asks the Commission to re-examine application of Procurement NBCs with the context of the full range of existing NBCs for CGDL, including PPP charges.

Table 1: CGDL NBCs

Line	Description of Applicable Surcharge	Non-Exempt CGDL PG&E E-20T ($/MWh) (1)	Non-Exempt CGDL SCE TOU-8-Sub ($/MWh) (2)	Cogen CGDL PG&E E-20T ($/MWh) (3)	Cogen CGDL SCE TOU-8-Sub ($/MWh) (4)
1	Public Purpose Program Charge (PPPC)	$3.92	$5.97	$3.92	$5.97
2	Nuclear Decommissioning Charge (NDC)	$0.38	$0.48	$0.38	$0.48
3	DWR Bond Charge (DWRBC)	$4.85	$4.85	$4.85	$4.85
4	DWR Power Cost Charge (DWRPC)[36]	-$4.27[37]	$5.50	-$4.27	$5.50
5	Competition Transition Charge (CTC)[38]	$2.63	$6.65	-	-
6	HPC/ECRA Charge[39]	$4.37	N/A	$4.37	N/A
7	**TOTAL KNOWN NBCs**	**$11.88**	**$23.45**	**$9.25**	**$16.80**
9	Procurement NBC	**unknown**	**unknown**	**unknown**	**Unknown**

These NBCs have a material impact on the assessment of development plans for a new cogeneration facility. Note, however, that the Procurement NBCs approved by the Commission in the several, above-mentioned decisions are not quantified on the table; indeed, they are unquantifiable. Nor are these charges

[36] DWRPC recovers the uneconomic portion of DWR's prospective power purchase costs.

[37] A "CDWR Power Charge" applicable to CGLD is no longer specified in PG&E's tariff; however, the PG&E Schedule E-DCG contains a "POWER CHARGE INDIFFERENCE ADJUSTMENT." The tariff states that the adjustment (either a charge or credit) is intended to ensure that customers that purchase electricity from non-utility suppliers pay their share of cost for generation acquired prior to 2003 (which presumably includes the CDWR power purchases). Indeed, value of this charge (and that of its predecessor the "CDWR POWER CHARGE") has ranged between -$5.00/MWh and $20.00/MWh during calendar year 2006.

[38] CTC recovers the cost of power purchase agreements, signed prior to December 20, 1995, in excess of proxy market price.

[39] SCE's Historical Procurement Charge (HPC) is determined on a customer specific basis and reflects the customer's cost responsibility for power costs incurred during the energy crisis. On March 1, 2005, the Energy Cost Recovery Amount (ECRA) superceded and replaced the Regulatory Asset (RA) Charge such that after March 1, 2005, applicable customers no longer incur additional RA Charges but instead incur Energy Cost Recovery Amount (ECRA) charges adopted by the Commission in Decision 04-11-015.

presented in any utility tariff. Consequently, it remains entirely impossible to estimate the potential impact of the Procurement NBCs on any CGDL project.

In general, all NBCs have a material effect on project economics; they all reduce the return on a project. For example, consider a customer generation project that has an installed cost on the order of $1,000,000/MW and an 11% internal rate of return.[40] Assume that the project is assessed only one NBC of **$5/MWh**[41], on Departing Load with a 90% load factor. Application of the $5/MWh NBC to that project will reduce the project's annual cash flows by about $39,400 per installed MW, [42] equaling a **47% reduction** in the internal rate of return. Moreover, a project with an initial **11% hurdle rate**[43] (a rate roughly equivalent to an IOU rate of return on equity) would require **a total return on investment** of about **20%** to compensate for a **$10/MWh** departing load exit fee and justify development.[44] In other words, the NBCs directly increase the cost of investment in cogeneration above the cost that would be faced by a utility installing the same facility.

These examples demonstrate the adverse impacts of CGDL NBCs on development consideration where the CGDL NBCs can be quantified. The

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[40] The rate of return that makes the present value of future cash flows equal to the initial capital investment.

[41] *C.f.,* Table 1, showing the current range of known applicable CGDL NBCs (depending on IOU and applicable tariff) from $9.25/MWh to $23.45/MWh.

[42] Multiply the dollar amount of the charge by total hours in a year and by the load factor to obtain the yearly per MW impact: 5 x 8760 x .9 = 39,420.

[43] The required rate of return in a discounted cash flow analysis, above which an investment makes sense and below which it does not.

[44] This calculation is performed in a spreadsheet and available by request.

problem is further exacerbated, however, when these charges cannot be quantified or are subject to material fluctuation.

b. Mere Declaration of Potential for A Procurement NBC Does Not Give CGDL Customers Notice Sufficient to Adequately Inform Customer Investment Decisions

Where, as in the case of the Procurement NBC, *the charge cannot be quantified*, it drastically complicates the planning process of utility customers. As noted above, in evaluating any investment, a prudent customer will perform a variety of economic analyses to determine whether the project meets its internal hurdle rate. A project that fails the internal hurdle rate analyses will not be developed by the customer. In order to properly perform the analyses to make this assessment, the customer must consider the anticipated costs associated with its decision to invest in the cogeneration project. NBCs are one clear category of costs associated with the customer's decision.

With "known" NBCs at the time of analysis, if there is a high level of volatility associated with the NBC (*e.g.*, the PPP NBC, particularly the CARE and CSI components), it is difficult to accurately assess their potential impact over time. In the case of an NBC that has not been (and indeed, cannot be) quantified, *i.e.,* the Procurement NBC, the customer's ability to accurately assess the project economics is perilously constrained. Cogeneration developers are left in the untenable position of being able to sufficiently quantify and manage fuel, financing and other project risks, but with no meaningful way to assess and mitigate the potential future impacts of NBCs. This result is inconsistent with

sound policy aimed at increasing regulatory certainty and encouraging investment in new generation resources.

Predictability of charges is, in fact, a policy basis for the legal requirement of notice. The legal principle of requiring prior "notice" of utility rates and changes is firmly established in the Commission's code. Indeed, Section 454 of the Commission's code requires that utilities seeking rate changes to provide its customers with notice (including "*the amount of the proposed rate change expressed in both dollar and percentage terms for the entire rate change. . . .*" [45]) Leaving aside all legal questions of the sufficiency of notice,[46] however, the **policy rationale** underlying the legal requirement of notice further compels this Commission to disallow application of the Procurement NBC to CGDL.

Giving "notice" of NBCs after development plans are made simply is not sufficient to inform the developer in assessing its options. It is critical that notice be provided with sufficient lead times for the development of generation projects. The lifecycle of cogeneration development could be as short as two years, but may span a longer period. Where the Commission approves the imposition of stranded cost surcharges on those customers that have already invested private funds to engage in customer generation, 45 day notice in a bill or notice in a Commission hearing dramatically and unfairly impacts, in a wholly unanticipated manner, project economics.

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[45] Pub.Util.Code § 454.

[46] EPUC reserves all rights to appeal the legality of any attempted application of a Procurement NBC to CGDL; a legal challenge to any attempted application of any Procurement NBC to CGDL should be anticipated.

Switching to customer generation requires both investment and the physical construction of generation resources. Creating the infrastructure necessary for customer generation projects requires the consideration of land use, procurement of equipment, labor and construction issues and obtaining numerous permits. The projects must also proceed in reliance that government approval for land use and air quality may be obtained. The actual development of a project can take 18 to 36 months from the initial stages to operation. Adequate notice should provide ample detail regarding the calculation of the charge and, logically, provide those affected by a rate change the opportunity to adjust their behavior to minimize the impact of any proposed changes. For these reasons, clear and complete notice and quantification of all NBCs prior to investment in customer generation is particularly important; the Procurement NBCs fail to provide this critical information and should not be imposed on CGDL.

2. Imposition of Procurement NBCs Unfairly Penalizes Customers Investing Private Capital in Cogeneration Dedicated to Serving California Load

Nonbypassable charges impose a penalty upon customers seeking to invest their own capital in a cogeneration resource. Not only must the customer bear its own investment costs, it must also bear the cost of utility investment and procurement. This penalty is patently inequitable in the case of the Procurement NBC, which asks the self-generating customer to pay expressly a portion of the capital costs of utility investments or utility procurement.[47]

[47] The Commission (and the IOUs) should also bear in mind that many of the CGDL customers remain on the IOU systems as bundled customers taking standby service. As bundled standby customers, these customers already pay their full and fair share of costs associated with IOU procurement.

Most troubling about the imposition of utility procurement costs upon cogeneration facilities is the fact that the customers in question have absolutely no control over the utility incurrence of the "stranded costs" associated with these charges.[48] CGDL customers are not allowed to review any of the data that is submitted in these applications.[49] The Commission does not engage in any cost comparison to evaluate whether such utility procurements are reasonable in light of other alternatives. Ultimately, the cogeneration facilities cannot engage in any kind of demand response efforts to lower their bills when all of the decision making is in the IOUs' hands.

This current NBC policy discourages private investment in the very resources which the state seeks to promote through legislation, EAP II and the IEPR. With no ability to control or even predict these costs, cogeneration facilities hesitate to commit private funds to increase generation in the state. This restriction adversely affects all ratepayers. Accordingly, the Commission must first reaffirm the mandated inclusion of CGDL data into IOU load forecasts, specifically large cogeneration facilities. The Commission must next revoke the

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[48] This troubling lack of control stems from the near-complete lack of access for cogeneration facilities to detailed IOU procurement information. Cogeneration facilities are barred from reviewing and assessing IOU procurement activities and are unable to participate in utility Procurement Review Groups. *See* D.06-06-066, at 70, OP 9 (barring market participants from access to confidential data); *see also* D.06-12-030, at 46, FOF 6, and 48, OP 1 (adopting a definition for Market Participating Party and categorizing EPUC as a market participant).

[49] *See, e.g.*, D.06-07-030, at 7 (adopting a revised benchmark methodology to address transparency concerns:"*Parties are left without information concerning the level of CRS applicable to their current consumption. The current method also relies on utility power purchaseand sales data which the utilities view as confidential and proprietary. Thus,* ***the relevant data are not made available to many of the parties that are responsible for paying CRS***.") (emphasis added)

authority of the IOUs to impose the Procurement NBC upon cogeneration facilities departing utility service to engage in customer generation.

B. Eliminating The Procurement NBC Would Encourage Cogeneration Development, Consistent With State Policy, And Provide A Reliable Solution To The State's Supply Needs

As discussed above, current NBC policy burdens the development process, both by adding uncertainty to the project analysis and increasing the difficulty of reaching an acceptable hurdle for rate of return. While elimination of all CGDL NBCs would completely eliminate this problem, the most critical element presented to the Commission in this Petition is the Procurement NBC. Prohibiting the application of the Procurement NBC to CGDL would substantially ease project development burdens and encourage the development of new cogeneration facilities. And increased cogeneration development would benefit the State in ways soundly recognized by this Commission, the Energy Commission and the Legislature.

1. Policymakers Have for Decades Expressed a Strong Preference for Cogeneration as a Supply Source

The State, speaking primarily through this Commission, has made a clear call for new generating resources to serve the state. A potential exists to meet that call, in part, through the development of new cogeneration resources located at key industrial sites around the State. The realization of that potential, in part, rests on Commission cogeneration policy.

Decision 06-07-029, issued on July 20, 2006, is the Phase I decision issued in the long-term procurement proceeding (R.06-02-013). This decision

finds that there exists a need for new generation.[50] In particular, it finds that PG&E has a need for 2,200MW of new generation and SCE has a need for 1,500MW of new generation.[51] Accordingly, it authorizes PG&E and SCE to procure these amounts of generation and to recover the net capacity costs in the form of an NBC such as the one authorized by D.04-12-048.[52] The decision notes its reluctance to adopt this procurement plan but states that such a plan is needed to ensure reliability and to ensure that no barriers remain to investment in new generation.[53]

In addition, the Commission has also voiced its view regarding the need to address supply issues in a way that minimizes utility capital investment. In its recent decision on demand response programs in the wake of the 2006 summer heat storm, the Commission observed that *"[p]ermanent load shifting can reduce the need for capacity investments, reduce the likelihood of shortages during peak periods and lower system costs overall by reducing the need for peaking units."*[54] The Commission further noted that "*permanent load shifting is not currently supported by the utilities' demand response budgets*." Installation of customer generation can work in the same way, reducing the need for utility capacity investments and reducing the likelihood of shortages.

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50 D.06-07-029, at 55 (Findings of Fact ¶¶12-14).

51 *Id*., at 54 (Finding of Fact ¶4).

52 *Id*, at 56-57.

53 *Id*, at 57 (Finding of Fact ¶22).

54 August 15 Peevey Ruling.

State policy has consistently and fully supported cogeneration as a solution to these supply problems. The Energy Action Policy II (EAP II) details:

> *a coordinated implementation plan for state energy policies that have been articulated through the Governor's Executive Orders, instructions to agencies, public positions and appointees' statements; the CEC's Integrated Energy Policy Report (IEPR); CPUC and CEC processes, the agencies' policy forums; and legislative direction*. [55]

Notably the EAP II lists cogeneration as one of its preferred energy sources.[56] In fact, the EAP II provides that "*[a]fter cost-effective efficiency and demand response, we rely on renewable sources of power and distributed generation, such as combined heat and power applications*." [57] The EAP II also includes the following as its recommended "key actions":

- *Provide for the continued operation of cost-effective and environmentally-sound existing generation needed to meet current reliability needs, including combined heat and power;*[58] *and*

- *Adopt a long-term policy for existing and new qualifying facility resources including better integration of these resources into CAISO tariffs and deliverability standards.*[59]

- Develop tariffs and remove barriers to encourage the development of Environmentally sound combined heat and power resources and distributed generation projects.[60]

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55 EAP II (issued on September 21, 2005), at 2, 7, 8.

56 EAP II, at 2, 7, 8.

57 EAP II, at 2.

58 EAP II, at 7.

59 EAP II, at 8.

60 Id.

In other words, the EAP II explicitly provides that use of energy from cogeneration resources should be given preference and recommends the integration of these resources in the future.

The statutes governing regulation by this Commission also reflect support for the development of cogeneration. Section 372(a), for example, provides that

> *It is the policy of the state to encourage and support the development of cogeneration as an efficient, environmentally beneficial, competitive energy resource that will enhance the reliability of local generation supply, and promote local business growth.*

Subsection (f) of this same statute goes on to provide the following, describing specific measures aimed:

> *To encourage the continued development, installation, and interconnection of clean and efficient self-generation and cogeneration resources, to improve system reliability for consumers by retaining existing generation and encouraging new generation to connect to the electric grid, and to increase self-sufficiency of consumers of electricity through the deployment of self-generation and cogeneration….*

In other words, the Commission's strong support for clean and efficient cogeneration energy is documented in its own statutory code.

Moreover, the California Energy Commission has enumerated the clear benefits which cogeneration provides to the State and the actions necessary both to preserve and encourage this critical resource. The Energy Commission's 2005 Integrated Energy Policy Report (2005 IEPR) expressly recognizes that:

> *Cogeneration, or combined heat and power (CHP), is the most efficient and cost-effective form of DG, providing numerous benefits to California including reduced energy costs, more efficient fuel use, fewer environmental impacts, improved reliability and power quality, locations*

> *near load centers, and support of utility transmission and distribution systems.*[61]

Of particular relevance to current Commission initiatives, the 2005 IEPR states that:

> *CHP effectively reduces greenhouse gas emissions and both transmission and distribution congestion. CHP facilities are located in local load centers where system operators often struggle to maintain local reliability. CHP also provides significant resources during peak demand periods, which help mitigate operational problems involved with meeting peak demand.*[62]

The Energy Commission notes that prior versions of the IEPR "*highlighted the importance of DG and CHP is meeting California's growing energy needs and providing and essential element of customer choice.*" [63] The Energy Commission also recognized however that "*[d]espite policy preferences, DG and CHP in California still struggle with major barriers to market entry in the context of traditional utility cost-of-service grid management*." [64] In summary, the Energy Commission concluded "*[c]urrent state policy must clearly change for California to take advantage of this valuable generation potential. It is equally important to retain the state's existing CHP that is so critical to the current reliable operation of the electric grid*." [65]

The preference for cogeneration resources as a means of meeting this State's supply requirements should come as no surprise. Cogeneration is a

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61 2005 IEPR, at 76.

62 2005 IEPR, at 80.

63 Id.

64 Id.

65 2005 IEPR, at 77.

reliable resource. It provides clean energy that furthers GHG reduction goals. Cogeneration also helps to alleviate congestion on the transmission grid and decreases the need for transmission upgrades. It conserves resources due to its proximity to load.[66] Cogeneration increases capacity within the state,[67] and improves system reliability.[68] Cogeneration could help address the energy shortages that have been memorialized in the August 15, 2006 Peevey Ruling and D.06-07-029. It also more efficiently utilizes natural gas to produce electricity[69] and can offer substantial environmental benefits.[70] Finally, excess generation associated with customer generated projects have the ability to help IOUs satisfy their procurement goals. For example, as a percent of total 2003 utility retained generation and QF energy purchases, cogeneration represents approximately 23% and 24% of PG&E's and SCE's 2003 totals, respectively.

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[66] Proximity to load conserves resources because there result generation losses when power is moved remotely to serve its load. For example, if the losses for power flowing over the utilities' wires are 7percent, 107MW of generation is required for every 100 MW of energy metered at the location where the energy is consumed. On the other hand, 100% of the power generated by self-generation can be used to serve on-site load. Onsite generation also allows local load to grow without the expense of expanded transmission and distribution investment.

[67] Historically California has been a net importer of power during peak demand periods. An infrastructure without barriers to customer generation can reduce the load on the system and thus California's reliance on out-of-state power.

[68] All things equal, a system comprised of many small generating units is more reliable than a system with a few large generation units. In a system where only a few large generating units exist, where even one of those generating units experiences an outage, it is likely to have a much greater impact on the system's reliability.

[69] Unlike a traditional boiler which produces only electricity, cogeneration equipment has the ability to use the same amount of natural gas to produce two forms of energy: electric and thermal. In addition, certain customer generation facilities, such as those located at a crude petroleum refinery, may be able to use waste fuels from the manufacturing process to further increase efficiency.

[70] The Warren Alquist Act, enacted by the California legislature in 1974, explicitly states in §25004.2 that, "*cogeneration technology is important with respect to the providing of a reliable and clean source of energy within the state and that cogeneration technology should receive immediate support and commitment from state government*."

2. Additional Cogeneration Could Contribute to the State's Current Need for New Supply

The Commission has called for material increases in capacity to meet the state's growing demand. The tables below highlight the most recent Commission approval for the acquisition or construction of capacity by the utilities:

Table 2

For SCE Customers	Amount of New Procurement (MW) Authorized to Be Collected through Procurement NBC	Estimated Installed Cost of Plant ($/kW)	Estimated Procurement NBC
Mountainview Power Plant[71]	1054	$682	unknown
D.06-07-029	1500	unknown	unknown
August 15, 2006 Peevey Ruling	250	unknown	unknown
Total:	2804	unknown	unknown

[71] Procurement NBC resulting from SCE's procurement of the Mountainview facility approved in D.03-12-059.

Table 3

For PG&E Customers	Amount of New Procurement (MW) Authorized to Be Collected through Procurement NBC	Estimated Installed Cost of Plant ($/kW)	Estimated Procurement NBC
Contra Costa 8 [72]	530	unknown	unknown
D.06-07-029; D.06-11-048	2250	unknown	unknown
August 15, 2006 Peevey Ruling	200	unknown	unknown
Total:	2980	unknown	unknown

In total, the Commission has seen a need for as much as 5784 MW of new capacity in the near term.

Interestingly, the IOUs' load forecast presented in R.02-01-011 which includes data and projections of CGDL indicates that by 2010, as a result of CGDL, PG&E had projected that its load would decrease by 1153 MW and SCE had projected a decrease of 1000 MW. This means that the need for (and costs of) new capacity could have been reduced by *about one third* if barriers to customer generation did not exist. In other words, had the utilities' own projections played out, private investment would have stepped in to ease the state's supply conditions.

[72] Procurement NBC resulting from PG&E's procurement of the Contra Costa 8 facility approved in D.06-06-035.

C. Elimination Of The Procurement NBC For CGDL Would Promote The State's GHG Objectives

This Commission has been actively engaged in the development of the state's GHG policy, material portions of which have been codified in Senate Bill (SB) 1368 and Assembly Bill (AB) 32. Cogeneration offers a means to bring GHG reductions to the state.

The Commission, through the Climate Action Team (CAT), identified Cogeneration Combined Heat and Power (CHP) as a concrete means of achieving GHG reductions. Specifically, the CAT Report articulated a strategy to encourage the development of CHP using various policy mechanisms.

> *These policy mechanisms may include regulatory incentives to encourage IOUs to promote customer and utility-owned CHP, changes to IOU rate design, market rules and regulations enabling easier access to wholesale markets, production tax credits for CHP, and other measures or incentives directed at key commercial and industrial activities in California.*[73]

The CAT Report targets reductions of GHG through new CHP at 1.1 million metric tonnes of CO_2 equivalent by 2010 and 4.4 million metric tonnes by 2020.[74]

Cogeneration CHP carries the potential to deliver greater results if the state's clear policies on cogeneration are given favorable practical effect. In the April 2005 Assessment of the California CHP Market, the CEC describes CHP as "*the most energy efficient and cost-effective form of distributed generation*"[75]; and as having, among other benefits, "*environmental benefits both in the reduction of*

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[73] Climate Action Team Report to Governor Schwarzenegger and the Legislature, March 2006, at 62.

[74] *Id.* at 61. It appears that these reductions may have been limited to smaller CHP installations under the Commission's Self-Generation Incentive Program.

[75] April 2005 Report at 1-1.

criteria pollutants and emissions of carbon dioxide that contribute to global warming." [76] These environmental benefits were quantified by a 2000 Energy Commission Report, in which it was estimated that cogeneration reduced CO_2 emissions by about 26 million tons per year on a regional basis.[77] A doubling of the existing cogeneration capacity (assuming retention of current capacity) could potentially double these significant GHG savings.

Member states of the European Union (EU) have recognized the benefits of cogeneration. As of August 2005, more than 50% of the total net electricity generation from Denmark came from CHP, or roughly 30 TWh of electricity annually; the Netherlands trailed at near 50%, or roughly 50 TWh annually.[78] In addition, also as of August 2005, several EU member states had adopted express CHP targets.[79] Poland, for example, had placed increasing obligations on energy companies that produce or trade electricity to purchase 16% from CHP by 2010. Germany, likewise, targeted 20 million metric tonnes of reduction due to the use of cogeneration between 1998 and 2010.

While California historically has showed similar support for cogeneration, current policy could cause the state to lag behind other world leaders in the use of this technology. Elimination of the Procurement NBC for CGDL – an

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76 *Id*. at 2-1.

77 Market Assessment of Combined Heat and Power in the State of California (2000).

78 EU ETS Phase II: Treatment of CHP, A Final Report to Defra, ILEX Energy Consulting, August 2005 (http://www.defra.gov.uk/Environment/climatechange/trading/eu/pdf/euetsphase2-treatmentchp.pdf) at 10.

79 *Id.* at 11.

unnecessary and unjustified exit fee – would be a step in the direction of securing the continued growth of cogeneration technology.

D. Any Justifiable Concern From The IOUs Concerning Stranded Procurement Costs Resulting From Installation Of Customer Generation Can Be Minimized Or Eliminated By Prudent Resource Planning

The Commission has been quick to apply NBCs to CGDL based primarily on the objective of avoiding cost-shifting. It is important to note that improper cost-shifting occurs only when a cost actually caused by one customer or class is shifted to another customer or class. EPUC submits that the Procurement NBC does not address costs that are caused by CGDL customers; with proper resource planning, as the utilities have always done, ongoing capital investments should not be "caused" by CGDL customers.

As discussed above, the notion that CGDL customers should be responsible for utility decisions to procure large amounts of capacity, such as a major power plant, is a relatively new idea. Historically, utilities were required to engage in prudent utility planning by, in part, forecasting load over time. Reasonably prudent forecasts included reflections of anticipated load growth and departing load. By employing a reasonable forecasting method, the utilities were able to avoid over-procurement for their load.

The Commission recognized this principle in D.03-04-030. In the initial "exit fee" proceeding in April 2002, agents for CDWR indicated that the 250 MW of annual forecasted CGDL assumption was utilized in calculating their revenue requirement. *"There are also explicit assumptions about **cogeneration** or*

distributed generation *in there also – about 250 megawatts a year in distributed generation coming on-line [which offset what was assumed in annual load growth during the 10-year modeling period]."* [80] Also at that workshop, agents for CDWR stated that, because Navigant did not procure on behalf of cogeneration and distributed generation that would depart the utility system over the 10-year period, it did not assume that CGDL and distributed generation customers would pay Cost Responsibility Surcharge exit fees.[81] This Commission sensibly adhered to this principal that since the departure of these CGDL customers was planned for, they should not pay the ongoing DWR Power Charge portion of the Cost Responsibility Surcharge.[82]

The utilities are fully capable of tracking material amounts of CGDL. Typically, if a customer is considering a large cogeneration installation, the utility is one of the first to know in light of the need to interconnect and plan for utility service. Most CGDL customers generally inform PG&E far in advance of their plans to install on-site generation, cogeneration and distributed generation. As PG&E's witness Mr. Wan explained in A.05-06-029, having previously worked for one of PG&E's larger CGDL customers, communication between the utility and the CGDL customer, particularly large customers, is ongoing:

> *Q Would it make sense to you if I told you that these customers [large power, CGDL customers] generally give PG&E a significant degree of*

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[80] A.00-11-038 *et al.* DWR Modeling Workshop, April 12, 2002, CDWR-Navigant/McDonald, Tr. WS 3, 237:7-19 (emphasis added).

[81] *Id.* at Navigant/McDonald, Tr. WS 3, 253:1-7.

[82] *See* D.03-04-030.

notice when they plan to install onsite customer generation; there is a significant amount of communication between them?

WITNESS WAN: A I believe that's possible, because that's what I used to do in my old job, too.

Q And it has not changed.

A That's right.[83]

With the regular and frequent level of communication between these customers and PG&E, PG&E should be able to forecast CGDL and plan to not serve the portion of these customers' load regularly met by the onsite generation. Moreover, the utilities actually track the installation and interconnection of distributed generation and cogeneration in their service territories.[84]

Critically, many of these customers continue to take IOU bundled service as standby customers. As standby service customers, they pay traditional, Commission-approved cost-of-service rates for IOU backup, supplemental, and maintenance power and services that they actually take under the IOU tariffed standby rate.

Forecasts of CGDL can be relied upon by the utilities in making their load forecasts. While the IOUs may not be 100% precise, a prudent utility should be able to balance 5, 10 or even 50 MW of CGDL without impacting the total service to their territory which can amount to about 18,000 MW of bundled load. Equally

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[83] A.05-06-029, 3 Tr. 258 (Wan, PG&E) March 2, 2006.

[84] *See*, *e.g.*, http://www.rule21.ca.gov/reports/Utility_DG_Activity_Reports/; http://www.rule21.ca.gov/reports/Utility_DG_Activity_Reports/SDGE%20DGPV%20Activity%20-%20Feb%202006.xls (link to San Diego Gas & Electric Company 2006 status report on interconnected distributed generation and cogeneration)*; see also* http://www.rule21.ca.gov/previous_meetings/2005_meetings/2005-12-14_meeting_72/SCE_DG_Status_as_of_11-30-05_public.xls (link to Southern California Edison Company's December 2005 status report on interconnected distributed generation and cogeneration*).*

as important, as ALJ Brown observed in the hearings held in A.05-06-029, a utility's own load growth can make up any "gap" created by departing load.

> *[ALJ Brown] Q: [H]as there been historic evidence that when there is departing load, it leaves a permanent gap that then is not filled by new customers? … How long is that 10-percent gap going to stay there? What are the projections?*
>
> *[Wan] A: Well, I – I think you – I am guessing that you are looking from the perspective of, uh, in a certain dimension, which is, like you said, 10 percent of the load goes away, maybe a few years later our entire service area – service territory can grow in such a time to absorb the 10 percent; is that the way you're looking at it?*
>
> *Q Yes. And then I'm wondering why that 10 percent would still be paying –*
>
> *A. Okay.*
>
> *Q -- when we now had enough new customers to be paying their fair share?*
>
> *A I – I think that's one dimension – way – one way to look at it.*[85]

PG&E's witness [Wan] tried to justify the imposition of departing load costs by noting that remaining customers would be paying more than those merely paying the departing load costs. ALJ Brown, however, was quick to observe the inequity that would result where an alleged gap did not remain permanent.

> *[Wan] A: But the remaining customers could be … paying more than depart[ing]- -- customers*
>
> *[ALJ Brown] Q:But that would be okay because I am thinking the ones who have left - - I could almost see your analysis with, if that 10 percent leaves and you have a total 10-percent gap … well, then it might not be fair for the bundled customers to pick up that 10-percent gap.* ***But what are the projections on how quickly that 10-percent gap is refilled?*** *… Because let's pretend* ***it's refilled in five years. Well, then, does it seem fair that those stranded customers are still – the departing customers are still paying for another 20 years when – when now***

[85] A.05-06-029, 3 Tr. 182-184 (Wan, PG&E) March 2, 2006 (emphasis added).

ratepayers really are indifferent? Because nobody's paying any more than they would have if those people hadn't left.

A Right. [86]

Indeed, where CGDL data is not considered, load growth can keep ratepayers indifferent when cogeneration facilities exit the utility system to produce their own energy. Of course, where the IOUs account for CGDL, any deleterious effect of CGDL on remaining customers can more effectively be limited.

If IOUs include CGDL data into their present forecasts, cogeneration facilities may be able to alleviate some of the energy shortage strain, potentially deferring utility investment. The IOUs could then better serve the needs of their customers. This result would be more in line with existing statutes and state policy.

In summary, the IOUs historically have incorporated data regarding CGDL when determining load forecasts and can continue to do so. Incorporation of CGDL information in utility load forecasts is consistent with the recommendation of the EAP II to encourage the use of combined heat and power. It also would accommodate the increased demand for electricity evidenced by the August 15, 2006 Peevey Ruling and D.06-07-029. More importantly, planning that includes this information into a utility's load forecast will eliminate the need to impose <u>any</u> stranded costs upon remaining customers. Finally, as discussed above, utilities are capable of managing small deviations from the forecasts and any gaps are likely to be filled by load growth. Accordingly, the utility companies should be

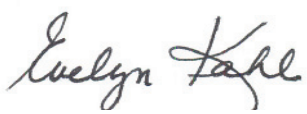
[86] A.05-06-029, 3 Tr. 184-185 (Wan, PG&E) March 2, 2006 (emphasis added); *see also*, *Id.,* at 187:7-15 (ALJ Brown *"what I'm suggesting, when that gap is filled with new customers, the long-term customers would still be indifferent because they … now have new people filling in that 10-percent gap?" "A I think that scenario can certainly happen.").*

required to integrate CGDL information into their load forecasts and their authority to impose a Procurement NBC upon CGDL should be revoked

V. CONCLUSION

The full benefits that cogeneration has to offer – as a secure, reliable supply and GHG reduction tool -- cannot be realized where Commission policy discourages customer generation. The Commission has before it the opportunity to remove an impediment to further development of cogeneration projects in California by prohibiting the application of the Procurement NBC to CGDL. Ratepayers can be protected from any cost shifting from departing customers to bundled customers if the IOUs are required to forecast CGDL on an ongoing basis.

Respectfully submitted,



Evelyn Kahl
Nora Sheriff

Counsel to the Energy Producers and Users Coalition

December 22, 2006

ATTACHMENT A

EXECUTIVE SUMMARY

EXECUTIVE SUMMARY

PETITION FOR MODIFICATION OF D.04-12-048 OF THE ENERGY PRODUCERS AND USERS COALITION

California ISO load has been curtailed four times in the past two years. Five years have passed since the energy crisis, and this state continues to need a significant amount of new, California-dedicated, reliable and efficient power generation. Growing concerns over global warming and legislated Greenhouse Gas (GHG) reduction programs demand that the needed new power generation help reduce GHG emissions. New and repowered customer cogeneration facilities -- funded, built and operated with private capital -- could help California meet these needs.

This Commission over the past decade has permitted utility recovery of departing load charges, or exit fees, under a variety of circumstances. Certain of these fees resulted from major policy transitions and crises. More recently, however, the Commission's concern about meeting the state's growing power needs, has acceded to utility demands for protection from nearly all risks in the normal course of the business of ongoing utility procurement. The protection takes the form of a nonbypassable charge, the Procurement NBC, to be assessed on all departing customers, including those installing onsite cogeneration facilities. Procurement NBCs have been granted for all three investor-owned utilities. Some have been facility-specific (*e.g.*, for Mountainview, Contra Costa 8, Humboldt, Colusa); others have encompassed entire Request For Offers (RFO) results (*e.g.*, for costs associated with all resulting power purchase agreements from SCE and PG&E RFOs). The unnecessary burden placed on customer cogeneration facilities by the Procurement NBCs, while protecting utilities from normal business risks, greatly reduces the likelihood of new and repowered customer cogeneration facilities. This perhaps inadvertent result of discouraging customer cogeneration development must be rectified.

Industrial customers with customer generation departing load (CGDL) already pay material nonbypassable charges that range from $9.25/MWh to $23.45/MWh, depending upon the time period, utility and applicable tariff. (See Table 1 in attached pleading.) Even with the current charges, these customers might be willing to invest significant private capital in new on-site cogeneration or repower existing sites but for the overwhelming risk of a Procurement NBC. The Procurement NBC's disincentive to private capital investment in cogeneration cannot be overstated.

The Procurement NBC has not been (and indeed, cannot be) quantified. In the face of the Procurement NBC, customers are simply unable to accurately assess the project economics. Without proper economic analysis for the new cogeneration investment, project development is burdened and hampered in its

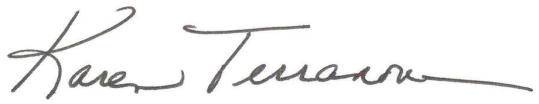
ability to compete for available internal capital. This outcome is inconsistent with California's needs and contrary to sound policies aimed at encouraging investment in reliable and energy efficient cogeneration resources, particularly those for which private capital – not ratepayer funds – is placed at risk.

The Procurement NBC should not be applicable to CGDL. Prudent utility planning historically has mitigated concerns regarding stranded utility costs and cost shifting. The utility should not be relieved in the normal course of business of this long-standing obligation to plan for CGDL. Prohibiting the application of the Procurement NBC to CGDL would substantially ease project development burdens and encourage the development of new, reliable cogeneration facilities. These facilities would then be able to: offer clean energy that further GHG reduction goals; help to alleviate transmission congestion; conserve resources due to proximity to load; increase capacity within the state; improve system reliability; and reduce the likelihood of shortages.

CERTIFICATE OF SERVICE

I, Karen Terranova hereby certify that I have on this date caused the attached **Petition for Modification of D.04-12-048 of the Energy Producers and Users Coalition** in R.04-04-003 to be served to all known parties by either United States mail or electronic mail, to each party named in the official attached service list obtained from the Commission's website, attached hereto, and pursuant to the Commission's Rules of Practice and Procedure.

Dated December 22, 2006 at San Francisco, California.



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